Supreme Court, U.S.
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No. 82-848

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

SERVICE MERCHANDISE COMPANY, INC.,
Petitioner,

v.

AMANA REFRIGERATION, INC. and
DAVIS-WATKINS COMPANY,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

BRIEF FOR RESPONDENT AMANA REFRIGERATION, INC. IN OPPOSITION TO PETITION

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Dated: January 17, 1983

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QUESTIONS PRESENTED

Respondent denies that the "*Questions Presented*" are as stated by Petitioner. Rather, Respondent asserts that the single, proper question presented is as follows:

> Did the court of appeals correctly affirm the district court's ruling that this case involved only non-price vertical restrictions to be tried to the jury under the rule of reason analysis mandated by *Sylvania?*

PARTIES TO THE PROCEEDINGS

Petitioner Service Merchandise Company was appellant below. Respondent Amana Refrigeration, Inc. was appellee below.

Amana Refrigeration, Inc. is a wholly-owned subsidiary of Raytheon Company. Other wholly-owned subsidiaries of Raytheon Company are: The Badger Company, Inc.; Beech Aircraft Corporation; Caloric Corporation; A.C. Cossor Limited (England); Electronics Nayarit, S.A. (Mexico); D.C. Heath, Canada, Limited (Canada); Iowa Manufacturing Company of Cedar Rapids, Iowa; Japanese Overseas Service, Inc.; Klasing G.m.b.H. (Germany); Heinz Kress G.m.b.H. (Germany); Kress Verwaltcngagesellschaft G.m.b.H. (Germany); Lexington-Electronic Realty Trust; Lexitron Corporation (Nevada); Lexitron Leasing, Inc.; Lexitron Marketing, Inc.; The Machlett Laboratories, Incorporated; Middlesex International Trade Corporation; PICCON, INC., Raytheon Air Control Company; Raytheon Air Control Company Mideast; Raytheon Aircraft Control and Landing Systems, Inc.; Raytheon Canada, Limited (Canada) Raytheon Educational Systems Company; Raytheon Engineering and Maintenance Company; Raytheon Europe International Company; Raytheon European Management Co., Inc.: Raytheon European Management and Systems Company; Raytheon Foreign Trade Company; Raytheon German Services Company; Raytheon Gulf Systems Company; Raytheon Halhleiter G.m.b.H. (Germany); Raytheon International Graphic Systems Company; Raytheon International Trade Company; Raytheon Leasing Corporation; Raytheon Logistics Support & Training Company; Raytheon Marine Sales and Service Company; Raytheon Middle East Systems Company; Raytheon Overseas Limited; Raytheon Procurement Company, Inc.; Raytheon Semiconductor

International Co., Raytheon Service Company; Raytheon Southeast Asia Systems Compay; Raytheon Submarine Signal Development Company; Raytheon Subsidiary Support Company, Inc.; Raytheon Systems Company; Raytheon Technical Assistance Company; Raytheon United Kingdom Limited; Raytheon Worldwide Company; Sedco Systems, Inc.; Seismograph Service Corporation; Speed Queen Company; Switchcraft, Inc.; TAG Semiconductors Limited; and United Engineers & Constructors Inc.

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The following abbreviations are used in this brief: "Tr." (trial transcript); "PX" (plaintiff's trial exhibit); "DX" (defendant's trial exhibit).

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On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

BRIEF FOR RESPONDENT AMANA REFRIGERATION, INC. IN OPPOSITION TO PETITION

Respondent, Amana Refrigeration, Inc. ("Amana") respectfully submits the Court should deny Service Merchandise Company, Inc.'s ("SMC") petition for a Writ of Certiorari seeking review of the Sixth Circuit's unanimous affirmance of the district court's judgment in this antitrust case brought by SMC attacking Amana's nonprice vertical restrictions in its product distribution system.

OPINIONS BELOW

The opinions of the United States Court of Appeals for the Sixth Circuit and the United States District Court for the Middle District of Tennessee are correctly cited in the petition.

JURISDICTION

Amana does not question the jurisdiction of the Court.

STATUTES INVOLVED

With respect to the statutes cited in the petition, Amana asserts that the only relevant statute is Section 1 of the Sherman Act (15 U.S.C. § 1).

STATEMENT OF THE CASE

This case arose out of the efforts of Amana, in the face of intense interband competition, to encourage its distributors and dealers to continue to provide valuable pre-sale, point-of-sale, and post-sale services in connection with the distribution and sale of Amana microwave ovens through vertical non-price restrictions universally imposed on its distribution system. These efforts were challenged by SMC, a catalogue showroom company, because SMC was unwilling to accept the responsibilities of becoming an authorized Amana dealer and was, therefore, unable to obtain an adequate supply of Amana microwave ovens after Amana's imposition of more effective non-price restrictions in reliance upon this Court's decision in *Sylvania*.[1]

SMC employes a "no frills" approach to marketing that relies heavily upon the "presold" aspect of brand-name

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[1] *Continental T.V., Inc.* v. *GTE Sylvania, Inc.*, 433 U.S. 36 (1977).

products. SMC prides itself on not providing pre-sale, point-of-sale or post-sale services such as trained sales persons, product demonstrations or cooking classes; nor does SMC display full model lines of a brand. Instead, SMC relies upon demand created by others to sell its brand-name goods. Accordingly, SMC is interested in offering for sale only certain models of highly promoted, brand-name products. TR. 125, 141-42, 193-96, 220, 1101-02, 1158-60.

Prior to 1978 Amana assigned each of its distributors an area of primary responsibility, but did not prohibit sales outside of the territory. PX 250. Amana's purpose in assigning distributorship territories was to encourage distributors and dealers to provide a high level of customer services and product promotion in an aggressive manner to meet interbrand competition.[2] TR. 2178-98. Amana deemed this marketing strategy essential to its success in the marketplace.

During the latter part of 1976, the Japanese manufacturers dumped a great number of microwave ovens on the United States market and, in a manner of weeks, Amana's dealer and distributor inventories built up to record levels. DX 28; TR. 2225-28. As a result of this product influx, many authorized dealers were willing to sell Ama-

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[2] Amana utilizes what SMC's marketing expert described as "a pretty wide-ranging, aggressive series of well-coordinated activities up and down the channel of distribution." SMC's marketing expert went on to acknowledge that exclusive distributorship territories promote interbrand competition by encouraging "a more aggressive selling from that distributor," thus making him "more effective in competition against its competitors." He also admitted that "strong intrabrand competition may reduce the propensity" of Amana distributors to engage in costly promotional activity. TR. 1117-18, 1093, 1147-48.

na microwave ovens to unauthorized, non-servicing dealers for resale outside the authorized dealer's sales area in order to claim certain promotional funds from Amana, while at the same time being relieved of the obligation to provide costly services to support the sale of those ovens. Transhipping, which previously had merely been a nuisance, became a serious interference with Amana's marketing strategy and threatened its survival in the microwave oven business. TR. 2228-32. "Transhipping" is known in the trade as a sale of products by an authorized distributor or dealer, often through what is known as a "diverter,"[3] to an unauthorized dealer for sale outside of the distributor's or dealer's area of primary responsibility so that his own market will not be adversely affected by the free-riding, unauthorized dealer.[4]

During this period, SMC was attempting to free-ride on the sales, service and promotional efforts of Amana distributors and dealers. Although SMC had access to several other brands of microwave ovens, SMC began, in 1976, to acquire Amana microwave ovens from diverters

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[3] A diverter is a broker of products whose purpose is to divert products to a destination or for a purpose different from what is represented when the products are purchased. TR. 124, 2980.

[4] A dealer would have little disincentive to sell to an unauthorized dealer in another market area who did not provide the required services. This was because the resulting loss of market development and the cost of customer and product services on transhipped goods was not a cost to the transhipping dealer but to the authorized dealers and distributor into whose territory the units were transhipped and retailed. Moreover, because the authorized dealer who transhipped and his distributor had been provided certain market development funds by Amana, they obtained a windfall on microwave ovens purchased from Amana but for which they would not incur market development and product support costs. TR. 2238-59.

after the Amana distributor in Nashville refused to supply it.[5] SMC wanted to sell the Amana microwave oven because of the demand that had been created by the costly efforts of authorized distributors and dealers and the post-sale product support, such as cooking schools, provided by Amana's authorized network, which services SMC refused to provide. By free-riding on the market development and product support services of others, SMC incurred lower costs associated with the sale and was usually able to sell the product at a lower price than an authorized dealer.[6] The reaction of the authorized dealers in the free-rider's area would be either to drop Amana products altogether, or to lessen substantially the quantity and quality of services. TR. 2237-38, 2271-74.

The sudden and significant increase in transhipping to non-servicing dealers, such as SMC, in 1976 and 1977 caused a marked reduction in the delivery of services provided by Amana's distribution system due to the free-rider effect. TR. 2225-39. Accordingly, Amana experienced a sharp decrease in its share of sales of domestic

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[5] For the same reason that transhipping to free-riders in *another* territory occurred, free-riding dealers were unable to purchase products from the distributor in their own territory. The distributor would not permit a dealer to free-ride upon him or the service-providing dealers in his territory, and for that reason refused to sell to such a free-rider. Thus, unauthorized dealers were unable to get products unless they could do it surreptitiously, perhaps through a diverter and always by transhipment.

[6] The unauthorized dealer could sell the Amana ovens at a lower price than the authorized dealers in his area because he purchased them at a lower price (since the selling-transhipping dealer profited from the receipt of development and product support funds without incurring development and product support costs) as well as because the unauthorized dealer does not provide pre-sale, point-of-sale or post-sale services. TR. 125, 1303-05, 2230-38, 2788-91.

countertop microwave ovens from 18% in 1976 to 11% in 1977. DX 23. Amana began to search for a method to halt this decline but it was advised that it would be imprudent to take any action because of the state of the antitrust law in early 1977. In October, 1977, in reliance upon the significant change in antitrust law announced in *Sylvania*, Amana imposed restrictions against selling outside one's assigned territory, dealer location restrictions and customer restrictions.[7]

After the implementation of these restrictions SMC and other free-riding dealers were unable to obtain an adequate supply of Amana microwave ovens because they either could not, or did not choose to, provide the required services. The restrictions have had the effect of substantially reducing transhipping and preserving the incentive to provide services. By confronting the free-rider problem with a change in its distribution system, Amana was able to stabilize and then to reverse its declining sales share trend. Amana's domestic sales share rose from 11% in 1977, to 12% in 1978, and to 13% in 1979.[8]

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[7] In October, 1977, and January, 1978, Amana changed its distribution system to assure that if product was shipped across territorial lines, promotional funds would be provided to service those products. Components of the system were: (1) exclusive territorial distributorships; (2) dealer location clauses; (3) dealer and distributor customer restrictions; and (4) transfer of promotional and service funds on transhipped products. PX 108, 115, 251; DX 27; TR. 2193-97, 2239-46, 2289-90.

[8] Amana's economic expert testified that in order to ascertain Amana's actual *market power* (distinguished from domestic sales share), one must necessarily take into account foreign microwave production by manufacturers who are now selling in the United States. One must also consider the number of units that could be shipped to the U.S. by foreign producers in the event the United States market became less competitive. Measuring market power accordingly, he calculated that Amana's market power expressed in terms of market share, was less than 10% in 1977, 1978 and 1979. This evidence was undisputed by SMC. DX 34; TR. 2594-2617.

SMC claimed that Amana's distribution system violated Section 1 of the Sherman Act. SMC alleged that the system is *per se* illegal in that it constitutes a group boycott of SMC, a scheme to enhance, maintain, or stabilize prices, a horizontal market division, or a *per se* illegal vertical restriction. SMC also alleged that the system is an unreasonable restraint of trade under the rule of reason. Amana denied that it distribution system was illegal or unreasonable under any theory.

Prior to trial, after the completion of discovery, Amana and SMC each filed motions for partial summary judgment. Amana's motion sought dismissal of SMC's four *per se* theories of liability. SMC's motion sought a judgment of liability upon the theories of group boycott, horizontal market division, price stabilization, and under the rule of reason. The district court denied SMC's motion and granted Amana's. In granting Amana's motion the court determined that, considering all of the evidence,[9] SMC could not make out a case of *per se* liability on any of these theories. The court determined that "in no material way . . . is [the case] distinguishable from [*Sylvania*]." 500 F. Supp. at 1248.

SMC was permitted to, and did, introduce in its rule of reason case before the jury all evidence it claimed supported its *per se* theories as probative of Amana's motive in imposing the vertical restrictions. 500 F. Supp. at 1249. The court's ruling on the summary judgment motions did not have the effect of excluding any evidence. At the close of all of the proof, SMC did not move for a directed verdict

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[9] In addition to the pleadings, depositions, exhibits and answers to interrogatories on file, SMC submitted several volumes of deposition extracts and documents obtained during discovery. The evidence SMC relies upon in its petition was before the court on the motions.

and the district court rejected SMC's request for jury instructions on each of its *per se* theories and again determined that the case should go to the jury only under the rule of reason mandated by *Sylvania*. After a seven-week trial, the jury returned a general verdict in favor of Amana and its distributor, Davis-Watkins Company.

SMC appealed its case and claimed error in the district court's action on both summary judgments, the district court's denial of *per se* instructions to the jury and the district court's jury charge. The Court of Appeals, in a unanimous decision, affirmed the trial court in all respects. The appellate court found that "no evidence exists to find that distributors and dealers joined together in unity of action to exclude SMC and that no evidence exists to find that Amana acted other than in its own economic interest. . . ." 686 F.2d 1199. It stated "there is no evidence of agreements between distributors or dealers to allocate markets" and "there is no evidence to support a finding of concerted action between Amana and its distributors or dealers for the purpose or with the effect of stabilizing the price of Amana microwave radarange ovens." *Id.* at 1201. It concluded "Amana's restrictions do not interfere with the setting of price by market forces but do require its distributors and dealers to sell the same product." *Id.*

REASONS FOR DENIAL OF THE WRIT

1. No Constitutional Issues Involved.

The petition does not set forth any issues requesting this Court to interpret or to apply the provisions of the United States Constitution. The petition is devoid of any Constitutional issues.

2. No Conflict With Prior Decisions Of This Court.

A. No Conflict With *Sylvania*.

This is a classic *Sylvania* case. It involves nothing more nor less than vertically-imposed, non-price restrictions in the form of territorial, location and customer restrictions, which were imposed by Amana universally on its distributors and dealers in order to assure that they would provide the valuable services necessary for Amana to be competitive in a highly competitive market.[10] The evidence of this was uncontradicted. The absence of any evidence of a *per se* violation and the overwhelming and uncontradicted evidence of vertically-imposed restrictions place this case squarely within the rule of *Sylvania*. The trial judge and the Court of Appeals so found. Reviewing the same evidence, the jury found that Amana's restrictions were reasonable and not anticompetitive.

SMC, in its appeal and now before this Court, attempts to twist what is without a doubt a *Sylvania* case into a *per se* case. SMC's theories in the context of the evidence, are nothing more than a challenge to the logic of *Sylvania*. To accept SMC's position would permit any antitrust plaintiff to avoid the logic of *Sylvania* by simply naming its case a *per se* case.

The weakness of SMC's argument is apparent. SMC now claims that it was denied its right to a trial by jury

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[10] It was uncontradicted that the microwave oven market is a highly competitive one. At the time that Amana imposed tighter restrictions in its distribution system, there were approximately 38 brands of microwave ovens being sold. TR. 2216. The uncontested evidence placed Amana's market share, properly measured, at less than 10% in 1977, 1978 and 1979. DX 34.

because of the trial court's refusal to permit the jury to consider its *per se* claims. SMC conveniently overlooks the fact that, in accordance with the district court's ruling on the motions for summary judgment, SMC was permitted to, and did, introduce all evidence it claimed supported its *per se* theories. In effect, SMC got two bites at the *per se* apple: one before trial on motion for summary judgment and a second after the close of proof when SMC requested the jury be given *per se* instructions. The district found before the trial, and again before charging the jury, that as a matter of law, the evidence presented did not make out a *per se* claim.

The crux of SMC's argument is that Amana's restrictions were intended to prevent price discounters from obtaining its products and this, without more, should convert the rule of reason analysis to a *per se* analysis on the theory that the restrictions are in fact a price-fixing scheme, or a boycott, or at least a horizontal allocation of territories. SMC has never been willing to admit that Amana's restrictions only discourage sales to free-riders—not to discounters—and make the market more competitive by making Amana more competitive with other manufacturers.[11] TR. 2245-46, 2261-62. *Sylvania*

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[11] SMC framed its price fixing theory as follows: "[T]he allocation of sales territories among Amana distributors and independent branches and the enforcement of the customer and location restrictions upon dealers was part of a scheme to prevent price competition between distributorship areas, both at the wholesale and retail levels, and to thereby stabilize prices within each distributorship area." 500 F.Supp. at 1250.

However, as the district court pointed out, SMC conceded in its response to Amana's summary judgment motion that Amana was not engaged in either resale price maintenance or price fixing. *Id.* SMC instead attempted to convert a vertical, non-price restriction into a *per se* violation by alleging that the restrictions enhanced price stabilization by restricting some aspects of intrabrand competition.

holds that a supplier has a legitimate interest in preventing "free riding." *Sylvania*, 433 U.S. at 54-59. A supplier such as Amana may utilize reasonable means to protect that interest. A ruling which characterized Amana's vertical restraints as *per se* illegal without submitting all the facts to a rule of reason test would ignore the teaching of *Sylvania*.

As the Court of Appeals emphasized, there is no evidence of any *per se* violation. All that SMC relies upon for its price-fixing and boycott theories are: (1) that SMC is known as a discounter; (2) that a few complaints of free-riding and the concomitant low price were made to Amana; and (3) that SMC did not obtain a sufficient supply of Amana ovens after Amana's imposition of its restrictions. SMC characterizes the complaints as "low price" complaints. In fact, as the evidence showed and the jury accepted, these complaints were directed towards SMC's free-riding.

The undisputed evidence was that Amana dealers do compete with each other intrabrand on price and service and many authorized Amana dealers are "price discounters," but these dealers provide the required services.

B. No Conflict With *General Motors*.

SMC's reliance upon *United States* v. *General Motors Corp.*, 384 U.S. 127 (1966) is misplaced. *General Motors* involved a horizontal conspiracy by the dealers who "roped in" the manufacturer to enforce the conspiracy. The concern underlying the *per se* approach in *General Motors* is that a manufacturer should not be permitted to facilitate a dealer cartel. As the court below found, nowhere in this record is there evidence of a dealer or distributor cartel.

SMC's argument is that distributors and dealers "voluntarily respected territorial lines and observed customer restrictions prior to January, 1978," but since the restrictions placed in the system in 1978 were a clarification and strengthening of the previous distribution system, the whole system is "necessarily horizontal." SMC's Court of Appeals Brief at 47-48. The evidence is that prior to 1978, Amana's agreements designated primary areas of responsibility; this was as much as the law was throught to permit. *United States* v. *Arnold, Schwinn & Co.*, 388 U.S. 365, 381 (1967). Although dealers and distributors were not restricted to sell only in their territories, they were required to devote their primary attention to that territory, and this requirement was imposed upon them by Amana as fully as the law permitted. TR. 2443-48. There was no evidence upon which SMC could rely to establish that Amana's territorial allocations originated with Amana's distributors who then "roped in" Amana to enforce an illegal horizontal market division.

The fact that a few dealers complained to Amana about SMC does not alter the vertical nature of the restrictions. Because a horizontal conspiracy among a manufacturer's distributors is not in the best interest of the manufacturer, a distributor-created horizontal conspiracy that involves the manufacturer can only be shown with proof that Amana was "controlled" by its distributors. *See, United States* v. *Topco Associates, Inc.*, 405 U.S. 596 (1972); *United States* v. *Sealy, Inc.*, 388 U.S. 350 (1967). SMC produced no such proof.

3. No Conflict With Other Courts Of Appeals Decisions.

The Sixth Circuit's decision does not conflict with the decisions of other courts of appeals. SMC submits that the lower courts' rulings conflict with *Cernuto, Inc.* v. *United*

Cabinet Corp., 595 F.2d 164 (3d Cir. 1979) and *Spray-Rite Service Corp.* v. *Monsanto Co.*, 684 F.2d 1226 (7th Cir. 1982), *petition for cert. filed*, 51 U.S.L.W. 3461 (U.S. Dec. 7, 1982) (No. 82-914). Amana insists that the Sixth Circuit appropriately followed *Sylvania*, and its holding does not conflict with *Cernuto* or *Spray-Rite*.

A. No Conflict With *Cernuto*

In *Cernuto* the Court of Appeals *assumed* that plaintiff could show that the manufacturer *terminated* him as a result of his competitor's complaints of low pricing. This assumption created, the court said, a "possibility" of a *per se* violation. The court made clear, however, that the use of a *per se* rule would be inappropriate if the termination was the result of defendant's own marketing strategy and judgment and was not motivated solely by considerations of price. 595 F.2d at 170.

In this case, the Sixth Circuit properly distinguished *Cernuto* rather than refused to follow it. As the court found, there was no such evidence as that assumed by the court in *Cernuto*. After three years of discovery and a full seven-week jury trial, SMC was not able to produce evidence to permit the inference of such a conspiracy.

B. No Conflict With *Spray-Rite*

The Seventh Circuit's opinion in *Spray-Rite*, although in our view incorrect, is not in conflict with the Sixth Circuit's opinion in the instant case. *Spray-Rite* involved a suit by a terminated distributor against its supplier-manufacturer. The Court of Appeals for the Seventh Circuit held that the terminated distributor may create an inference of a conspiracy to fix prices sufficient to go to the jury by showing that the manufacturer received complaints about plaintiff's pricing from other distributors and, *in response*, terminated plaintiff.

The instant case is different in two respects: (1) It involves not the termination of a "discount" distributor, but the nationwide application of Amana's marketing strategy to discourage sales to free-riders; and (2) there was no evidence that the imposition of the restrictions emanated from any source other than Amana. The undisputed proof was that Amana instituted its restrictions in response to the decline in sales share caused by the reduction in services resulting from free-riders who obtained the product by transhipment.

CONCLUSION

SMC's petition is a challenge to *Sylvania*. Unwillingness to acknowledge the authority of *Sylvania* pervaded its motion for summary judgment, its conduct at trial, its dissatisfaction with the jury instructions, its position on appeal to the Sixth Circuit and its request for a Writ of Certiorari.

The Sixth Circuit's decision properly follows *Sylvania* and there are no compelling reasons for this Court to grant the writ.

Respectfully submitted,

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